



# ARIZONA STATE RETIREMENT SYSTEM

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Paul Matson  
Director

## SUMMARY OF THE PUBLIC MEETING OF THE ARIZONA STATE RETIREMENT SYSTEM (ASRS) INVESTMENT COMMITTEE

HELD ON  
Monday, February 14, 2011

2:30 p.m.

The Arizona State Retirement System (ASRS) Investment Committee (IC) met at 3300 N. Central Avenue, 14<sup>th</sup> Floor, Phoenix, AZ 85012. Mr. Tom Connelly, Chair of the IC, called the meeting to order at 2:30 p.m.

### 1. Call to Order; Roll Call; Opening Remarks

Present: Mr. Tom Connelly, Chair  
Mr. Christopher Harris, Vice Chair (via telephone conference call)  
Mr. Larry Trachtenberg (via telephone conference call)  
Prof. Dennis Hoffman (via telephone conference call, for first hour of meeting)

A Quorum was present for the purpose of conducting business.

### 2. Approval of Minutes of the December 15, 2010 Public IC Meetings

**Motion:** Mr. Larry Trachtenberg moved the minutes of the December 15, 2010 Public IC meeting be adopted. Mr. Christopher Harris seconded the motion.

By a vote of 4 in favor, 0 opposed, 0 abstention and 0 excused, the motion was approved.

### 3. Presentation, Discussion, and Appropriate Action Regarding the ASRS Investment Policy Statement (IPS)

Mr. Paul Matson began the discussion by giving a brief introduction on the subject. Mr. Matson indicated that the IPS is an in-house document produced by staff; bringing together existing documentation into one cohesive standardized policy with the inclusion of additional relevant sections. Mr. Matson stated that though this is not a required document, in his opinion, it is consistent with good governance. Mr. Matson also stated that this document was previously presented to the IC on December 15, 2010. At that time, the IC requested the three consultants: Meketa, NEPC and Townsend provide commentary to this document. This has been completed and all three consultants are in agreement with this final document.

Mr. Matson noted an error brought to his attention by a Trustee in the first sentence on page 4 of the IPS in that it omitted the word "not"; the paragraph should read:

*"The ASRS strives to maintain an efficient and relatively low aggregate investment management fee structure...the ability to access market capital opportunities which may not be available through ASRS internal investment program."*

Mr. Connelly asked Mr. Matson, “In your opinion, does this statement encompass the duties of, or the items that the Trustees should be looking for, to monitor, or discuss throughout the year? Would you say it is, all inclusive, or mostly inclusive?” Mr. Matson responded that it is mostly inclusive, but fiduciaries should not limit their oversight, further stating that this document is to be used in concert with the Board Governance Policy Handbook.

Mr. Connelly added that he would like a review of the IPS as part of the IC Annual Responsibilities Report.

Mr. Harris concluded that this was a well-thought out document and provides continuity, adding further that he supported the document. Mr. Connelly agreed that he is comfortable with this document in that over time it can evolve.

**Motion:** Mr. Larry Trachtenberg moved that the IC recommend to the full Board the approval of the ASRS Investment Policy Statement. Mr. Christopher Harris seconded the motion.

By a vote of 4 in favor, 0 opposed, 0 abstention and 0 excused, the motion was approved.

#### **4. Presentation, Discussion, and Appropriate Action Regarding the ASRS Opportunistic Private Investment (OPI) Plan**

Mr. Paul Matson began by stating the ASRS OPI Program was initially approved by the Board in July 2011. As a result, an initial version of the OPI Program Plan was developed and presented to the IC on December 15, 2010. Since the initial presentation the document has been reformatted to be consistent with the format of the ASRS Real Estate and Private Equity Strategic Plans. In addition, ASRS’ three (3) consultants (Meketa, NEPC and Townsend) have reviewed the document and have concurred with its appropriateness and support its adoption.

Mr. Matson briefly reviewed the document, noting Mr. Polen, Portfolio Manager of Private Markets; revisions were the result of the full Board’s review of the Plan on December 17, 2010. Mr. Polen stated that Plan revisions focused on an expansion of governance roles and responsibilities; bringing it in-line with comparable standards of the Real Estate and Private Equity plans.

Mr. Larry Trachtenberg, Mr. Matson, and Mr. Polen engaged in conversation regarding the definition of due diligence. Mr. Christopher Harris raised the question whether the ASRS may waive investment due diligence. Mr. Polen commented that the IMD would not waive due diligence, however, discretion to use other analyses done by other limited partners (LPs), other investors or internal staff makes sense and would be at the discretion of the asset class committees.

Mr. Connelly commented that due diligence is not done in a vacuum and supports the use of external parties’ analyses when available to help the ASRS make investment decisions. Mr. Harris concurred. Mr. Trachtenberg indicated that the language could be better refined to remove any ambiguity regarding this matter. Mr. Matson agreed that verbiage modification would be made to the OPI Plan.

Mr. Harris requested that under the Defined Roles of Decision Making Bodies that the second bullet point under Duties of the IC be modified for clarity to include the word “Asset Class”, to read “provide expert advice to the Board and Asset Class Committee.” Mr. Matson concurred and requested this modification be made in the document that will be presented to the full Board on February 18, 2011.

Discussion of the Governance Structure section of the OPI plan ensued focusing on the sentences, "Because of the unique character of investments which will be considered for the OPI program, OPI will not have a single, dedicated consultant. Rather consultants will be selected and receive assignments at the discretion of the committee to which a particular investment is assigned". Mr. Harris requested clarification of his interpretation that asset class committees will select the consultant. Mr. Matson affirmed that this is the correct interpretation.

Mr. Harris concluded by stating that overall, this is a good document that has progressed well. Mr. Connelly further noted that all consultant feedback on the document has been completed and comments have been addressed to their satisfaction. Ms. Jennifer Young, The Townsend Group and Mr. Jess Downer, Meketa both agreed via telephone conference call. Mr. Dan LeBeau, NEPC, affirmed support of the document in person.

**Motion:** Mr. Christopher Harris moved that the IC recommend to the full Board the approval of the Revised Opportunistic Private Investment (OPI) Strategic Plan *with modifications discussed and agreed to by the Committee*. Mr. Lawrence Trachtenberg seconded the motion.

By a vote of 3 in favor, 0 opposed, 0 abstention and 1 excused, the motion was approved. (Note: Prof. Dennis Hoffman exited the conference call during the presentation and discussion of this agenda item.)

## **5. Presentation, Discussion, and Appropriate Action Regarding the ASRS Investment Disclosure Policy (IMD SOP034)**

Mr. Paul Matson introduced the agenda item, stating that he and staff had been working on this for some time, adding that it had previously been an expansive set of documents but has been consolidated with the intent to clarify and simplify in order to ensure compliance to procurement standards, laws, and good practice. Mr. Matson stated that staff has attempted to simplify the implementation of the Disclosure Policy in order to better ensure understanding and compliance.

Mr. Matson first noted a request from Mr. Alan Martin, NEPC to revise (noted in red text) the Paragraph 1 of the Background statement on the Memorandum to the Investment Committee, dated February 2, 2011:

*"... "Placement Agent Disclosure" policy was reviewed and revised to clarify the roles and responsibilities for obtaining disclosure information from ASRS staff, Trustees, and placement agents **acting on behalf of managers retained by ASRS.**"*

The Committee agreed that this addition better clarified the background statement.

Mr. Trachtenberg requested Mr. Matson clarify the forms, specifically the yellow highlighted section of the Conflict of Interest Disclosure Form. Mr. Matson reviewed both IMD SOP034 and the forms; explaining that the purposes of the yellow highlighted section on the form addresses any gray areas or questions that may arise. Mr. Matson added that the policy can be revised at any future date to further modify the forms, or any other part of the document.

Mr. Matson listed his suggested revisions:

1. Page 2, number the sequentially underlined section headings, and
2. Remove the Cc: line from the Investment Procurement Search and Private Market Decision Confidentiality and Disclosure Form,

The Committee concurred, and discussion continued.

Mr. Harris, referring to IMD SOP034, Page 2, **Investment Consultants**, first bullet point: *"Disclosure of the investment manager engagement of current, prospective direct or indirect placement agents for any activity from 12 months prior to the date of the recommendation,"* questioned if 12 months was a long enough time period, suggesting perhaps an 18 to 24 month period. Mr. Matson indicated that extending the time period could be accomplished. Given Mr. Dan LeBeau, NEPC, was present the Committee asked his opinion on NEPC's protocol. Mr. LeBeau agreed with 18 months, however, stated that he would have to confirm this with the NEPC Compliance Officer. Mr. Matson asked Mr. Le Beau to confirm and report his findings to Mr. Dokes. Additionally, Mr. Matson asked the two consultants attending via telephone conference call, Mr. Jess Downer, Meketa, and Ms. Jennifer Young, The Townsend Group, to as well report their firms recommended protocol to Mr. Dokes.

Mr. Connelly noted that a motion is not necessary, only the Committee's acceptance of the policy.

**Motion:** Mr. Christopher Harris moved that the IC accept the updated SOP034 as presented *with modifications discussed and agreed to by the Committee*. Mr. Lawrence Trachtenberg seconded this motion.

By a vote of 3 in favor, 0 opposed, 0 abstention and 1 excused, the motion was approved.

## **6. Presentation, Discussion, and Appropriate Action Regarding the ASRS Supplemental Retirement Savings Plan (SRSP)**

Mr. Matson stated that the SRSP was developed and implemented after the DROP program was repealed. The SRSP is governed by IRS statute 401(a), making it a very structured program in that, (1) contributions are fixed in perpetuity for the career of the employee with their current employer and (2) an employee has only a two-year window to decide if they want to participate in the plan.

Mr. Matson briefly described the very different, more flexible and newer Supplemental Salary Deferral Program (SSDP) which is regulated by IRS statutes 403(b) and 457.

Mr. Matson noted that the Board approved both the SRSP and SSDP Plan documents which delegated to the Director and staff the oversight of both investment programs and the vendor selection/de-selection process. Mr. Matson noted the Board Governance policy requires the IC to annually review these programs and report doing so to the Board as one of its annual responsibilities.

Mr. Pat Klein presented both programs in concert noting that though very different programs the manner in which the ASRS promoted and rolled the programs is very similar. Mr. Klein reiterated Mr. Matson's previous summary of the two plans. Mr. Klein noted that the SRSP contract was awarded to Nationwide in 2006. Further noting the SRSP has been in place for five years, and the contract with Nationwide is coming to end. As such, a Request for Proposal will be forthcoming.

Mr. Klein provided a brief summary of plan participation, and reviewed the attachments stating that the reports provide a snapshot of the plan demographics and performance, stating that Mr. Dokes would speak in greater detail to the investment aspects. Mr. Klein referenced the attachments and their relation to the overall implementation and management of the programs.

Mr. Dokes provided a brief overview of the investment fund options which are administered by Nationwide.

#### **7. Presentation, Discussion, and Appropriate Action Regarding the ASRS Supplemental Salary Deferral Program (SSDP)**

Mr. Klein provided a brief history of the SSDP plan, noting the legislature authorized the ASRS to put forth this program and a contract was awarded in February 2010 to TIAA-CREF. Mr. Klein gave a brief synopsis of the plan to date, noting participant eligibility and restrictions. Providing a review of the program participation and performance, Mr. Klein referenced the attachments.

Mr. Dokes provided a brief overview of the program's performance and fund offerings. Mr. Dokes noted the report format will likely be modified to better display and contain the most relevant fund performance information. Mr. Connelly asked if there was any intent to change the roster (fund managers) in either of the Plans. Mr. Dokes stated that no manager/fund roster changes are anticipated to be made at this time.

#### **8. Presentation, Discussion, and Appropriate Action Regarding Director's Asset Class Committee Update**

Mr. Dokes stated that three asset class committee meetings have occurred since the last IC meeting; one REC, one PEC and one PMC. Mr. Dokes cited the discussion items for each asset class committee.

#### **9. Presentation, Discussion, and Appropriate Action Regarding the Investment Management Division's (IMD) House Views**

Mr. Gary Dokes began the discussion by referring to the provided ASRS Daily Market Value Report; noting that in the broad public market sectors the ASRS is tactically underweight (to policy) in fixed income and overweight (to policy) in U.S. and non-U.S. Equities.

Mr. Dokes commented that three asset class rebalancing's are currently underway or may occur over the next few months. These are primarily the result of the Total Fund Rebalancing Committee's assessment of relative value between asset classes or between ASRS actual asset class holdings vs. their respective Strategic Asset Allocation (SAA) Policy weights.

More specifically:

1. Transition approximately 1% of ASRS Small (SC) and Mid-Cap (MC) Equities to Large-Cap (LC) Equities. Rationale: De-risking, relative value equity sub-asset rebalancing decision which will reduce a portion of ASRS tactical SC/MC overweight relative to its SAA policy.
2. Tactically fund the remaining balance of ASRS Commodities 3% SAA Policy (i.e., approx 1.3%). Rationale: Migrate to SAA policy allocation and continued secular demand for commodities. Implementation bias to fund incrementally in anticipation of possible near-to-intermediate term aggregate commodity market price pull-back (due to seasonality and Q3/Q4 2011 rapid price movement).
3. Transition approximately 1% of ASRS High Yield (HY) exposure to short-to-intermediate government bonds and Mortgage Backed Securities (MBS). Rationale:

De-risking, relative value fixed income rebalancing decision. CY10 HY Index performance of 15% was more than double of Core Bond Index performance; HY credit spreads (and all-in yields) continue to narrow approaching all-time tights relative to Treasuries. Reducing ASRS actual HY allocation from its fully funded 2% SAA policy allocation is prudent in light of possible HY profit-taking and in anticipation of heavy HY paper issuance.

Mr. Connelly asked IC members if they had any questions; none were noted.

## **10. Future Agenda Items**

Mr. Dokes stated that some future IC agenda topics include but are not limited to:

1. Governance Handbook
2. Sourcing of Private/Public Investment Opportunities
3. Total Fund Rebalancing Process
4. IMD/IC Investment Symposium
5. CIO Risk Management Tools
6. Investment Beliefs

Mr. Larry Trachtenberg asked that the topic of hedge funds be discussed. Mr. Dokes replied that he intended to address hedge funds, in addition to other absolute return strategies, during the Investment Beliefs agenda item discussion.

Mr. Dokes concluded by stating that as part of consulting consolidation process over the next couple months the ASRS GTAA Program consulting support services will migrate from Mercer to NEPC.

## **11. Call to the Public**

No members of the public requested to speak; the meeting adjourned at 5:22 p.m.

Respectfully submitted,

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Regina Landeros-Thomas, Secretary Date

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Gary Dokes, Chief Investment Officer Date